

Message Text

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ACTION EUR-12

INFO OCT-01 EA-09 NEA-10 IO-13 ISO-00 AID-05 CIAE-00
EB-08 FRB-01 INR-07 NSAE-00 USIA-15 XMB-04
OPIC-06 SP-02 LAB-04 SIL-01 OMB-01 NSC-05 SS-15
STR-04 CEA-01 AGRE-00 /124 W
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P R 301106Z MAR 77
FM AMEMBASSY LONDON
TO SECSTATE WASHDC PRIORITY 2099
TREASURY DEPT WASHDC PRIORITY
INFO AMEMBASSY BONN
AMEMBASSY BRUSSELS
AMEMBASSY DUBLIN
AMEMBASSY NEW DELHI
AMEMBASSY PARIS
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AMCONSUL BELFAST
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DEPARTMENT PASS FEDEARL RESERVE BOARD

TREASURY FOR DONALD E. SYVRUD, OASIA

E.O. 11652: N/A
TAGS: ECON, UK
SUBJECT: ECONOMIC FORECASTS IN THE CHANCELLOR'S MARCH 29
BUDGET

1. CHANCELLOR OF THE EXCHEQUER HEALEY REVIEWED THE STATE
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OF THE ECONOMY AND ITS MEDIUM-TERM PROSPECTS IN HIS
MARCH 29 BUDGET MESSAGE. HE VIEWED THE NEAR-TERM PROS-
PECTS AS HARSH.

"IF WE WERE TO MAKE NO CHANGE WHATEVER IN PRESENT
POLICIES, I WOULD SEE THE PROSPECTS AS FOLLOWS. PRODUC-
TION WOULD GROW ONLY SLIGHTLY IN THE NEXT TWELVE MONTHS. /
THE MAIN INCREASES IN DEMAND ARE LIKELY TO BE IN NET EX-

PORTS AND MANUFACTURING INVESTMENT - THE SECTORS WHICH WE WANT TO LEAD THE RECOVERY OF THE ECONOMY. FROM OTHER SECTORS, HOWEVER, LITTLE OR NO STIMULUS IS TO BE EXPECTED. PUBLIC EXPENDITURE ON GOODS AND SERVICES WILL BE RATHER LOWER THAN LAST YEAR. AND, ON PRESENT POLICIES, I WOULD EXPECT NO INCREASE IN PRIVATE CONSUMPTION. INDEED, THERE MIGHT BE SOME DECLINE.

"TAKEN TOGETHER, THESE TRENDS COULD BE EXPECTED TO MEAN THAT DEMAND AND PRODUCTION WOULD CONTINUE TO GROW SLOWLY. BUT WITH SO MODEST A RECOVERY IN OUTPUT I WOULD NOT EXPECT ANY FALL IN THE LEVEL OF UNEMPLOYMENT. INDEED, I FEAR SOME FURTHER RISE WOULD BE MORE LIKELY. THE RATE OF INCREASE IN UNEMPLOYMENT HAS, HOWEVER, BEEN FALLING MARKEDLY. BUT TWO MONTHS IS TOO SHORT A PERIOD ON WHICH TO FORM A JUDGEMENT. THE PLAIN FACT IS THAT THE PRESENT LEVEL IS UNACCEPTABLY HIGH; AND ACTION IS CLEARLY NEEDED TO IMPROVE THE FUTURE PROSPECT."

2. HE NOTED AS WELL THE DIFFICULTY OF RESTRAINING PRICE INCREASES LAST YEAR IN THE FACE OF A DEPRECIATING CURRENCY, BUT ASSERTED THAT A THIRD ROUND PAY AGREEMENT COULD ALLOW A FALL OF THE INFLATION RATE INTO SINGLE DIGITS BY THE SECOND QUARTER OF 1978. HE FRANKLY SAW THAT THERE WAS NO CHANCE OF OBTAINING SUCH AN AGREEMENT UNLESS PRICE CONTROLS WERE STRENGTHENED AND ANNOUNCED THE INTENTION OF PREVENTING "ANY UNREASONABLE PROFIT MARK-UP, BY KEEPING THE PRICE CONTROL ON PROFIT MARGINS, AND BY TAKING A NEW POWER TO FREEZE A PARTICULAR PRICE FOR UP TO A YEAR WHEN AN INDEPENDENT INVESTIGATION SHOWS

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THIS TO BE JUSTIFIED." AT THE SAME TIME THE NEED TO AVOID DAMAGING THE RATE OF RETURN ON INVESTMENT WAS ACKNOWLEDGED.

3. THE EXTERNAL SECTOR WAS THOUGHT TO HAVE GOOD NEAR-TERM PROSPECTS. NORTH SEA OIL WOULD BRING THE CURRENT ACCOUNT INTO A HEALTHY SURPLUS BY THE FIRST HALF OF 1978. THE CAPITAL ACCOUNT ALSO APPEARS HEALTHY AS THE DECEMBER MEASURES, THE IMF AGREEMENT, THE BASLE AGREEMENT ON STERLING BALANCES, AND THE MEASURES TO STOP THE STERLING FINANCE OF THIRD COUNTRY TRADE CONTRIBUTED TO SUBSTANTIAL INFLOWS THIS YEAR. THE CHANCELLOR HOWEVER STRESSED AGAIN THAT FORESEEABLE DEFICITS WOULD NOT BE FINANCED BY PRIVATE STERLING INFLOWS, CITING THE MEDIUM-TERM EUROCURRENCY LOAN AS CARRYING OUT THIS PLEDGE.

4. M3 WILL PROBABLY SHOW A GROWTH RATE TO MID-APRIL 1977 WHICH IS AT THE BOTTOM OF THE EARLIER FORECAST 9 TO 13 PERCENT, OR BELOW. IN THE COMING YEAR, AN M3 TARGET OF

9 TO 13 PERCENT HAS BEEN SET AGAIN.

5. THE PUBLIC SECTOR BORROWING REQUIREMENT FOR THE FINANCIAL YEAR NOW ENDING IS CURRENTLY ESTIMATED AT 8.8 BILLION POUNDS, AND IF CURRENT POLICIES WERE CONTINUED IT WOULD

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P R 301106Z MAR 77

FM AMEMBASSY LONDON

TO SECSTATE WASHDC PRIORITY 2100

TREASURY DEPT WASHDC PRIORITY

INFO AMEMBASSY BONN

AMEMBASSY BRUSSELS

AMEMBASSY DUBLIN

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BE FORECAST TO BE 7.5 BILLION POUNDS IN THE 1977/78 FINANCIAL YEAR. THE TAX CUTS REPORTED IN A SEPTEL ARE FORECAST TO RAISE THE 1977/78 PSBR TO 8.5 BILLION POUNDS, HOWEVER.

6. THE IMPACT ON THE ECONOMY THAT CHANGES IN THE BUDGET

AS WELL AS CHANGES IN THE GOVERNMENT'S VIEW OF KEY SEC-
TORS ARE LIKELY TO HAVE, MAY BE ASSESSED BY COMPARING
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THE FORECASTS PREPARED FOR LAST DECEMBER'S MINI-BUDGET
WITH THE ONES PREPARED FOR THE MARCH 29 PRESENTATION.

ECONOMIC PROSPECTS FOR 1977

DEC. 26 MARCH 29
FORECAST FORECAST

A. OUTPUT AND EXPENDITURE AT CONSTANT
PRICES; PERCENT INCREASE 2ND HALF

1976 TO 2ND HALF 1977

GDP (AT FACTOR COST)	2	1-1/2
CONSUMER EXPENDITURE	-2	-1
PUBLIC EXPENDITURE ON GOODS AND SERVICES	-3	-1-1/2
EXPORTS OF GOODS AND SERVICES	8-1/2	5-1/2
PRIVATE FIXED INVESTMENT	-	1
IMPORTS OF GOODS AND SERVICES	1-1/2	2

B. BALANCE OF PAYMENTS ON

CURRENT ACCOUNT: BILLIONS OF POUNDS

1977 1ST HALF	-1	-1/2
1977 2ND HALF	-	1/2
1978 1ST HALF	N.A.	1/2

7. THE REAL GROWTH IN THE ECONOMY IN CALENDAR YEAR 1977
OVER CALENDAR YEAR 1976, AND THE FIRST HALF OF 1978 OVER
THE FIRST HALF OF 1977 IS FORECAST IN THE MARCH MESSAGE

AS: 1ST HALF 1978

1977 OVER	OVER	
1976 1ST HALF 1977		
CONSUMER EXPENDITURE	-1/2	1/2
PUBLIC EXPENDITURE ON GOODS AND SERVICES	-1/4	-2
PRIVATE FIXED INVESTMENT	-	7
EXPORTS OF GOODS AND SERVICES	7	5-1/2
IMPORTS OF GOODS AND SERVICES	5-1/4	2
GDP (AT FACTOR COST)	1-1/4	1-1/2

8. OTHER FORECASTS:

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PERCENT CHANGE IN RETAIL PRICES:

FOURTH QUARTER 1976 TO FOURTH QUARTER 1977 13

SECOND QUARTER 1977 TO SECOND QUARTER 1978 9-1/2

PUBLIC SECTOR BORROWING REQUIREMENT (BILLION POUNDS)

FINANCIAL YEAR 1976-77 9
FINANCIAL YEAR 1977-78 8-1/2

9. THE CHANCELLOR WENT BEYOND THE NEAR-TERM ASSESSMENTS TO FOCUS ON SOME MEDIUM-TERM PROBLEMS WITH WHICH THE U.K. MUST GRAPPLE. THE FIRST SUCH PROBLEM IS THAT IT IS NECESSARY TO SECURE A SUBSTANTIAL CURRENT ACCOUNT SURPLUS IN THE FUTURE TO ALLOW REPAYMENT OF CONSIDERABLE INTERNATIONAL DEBT, "THE PRECONDITION FOR RESTORING ECONOMIC INDEPENDENCE." NORTH SEA OIL WILL NOT PRODUCE SUFFICIENT REVENUE TO ALLOW SUCH A SURPLUS TO BE ATTAINED SIMULTANEOUSLY WITH FULL EMPLOYMENT IN THE CONTEXT OF THE CURRENT ECONOMIC STRUCTURE. IT SHOULD BE POSSIBLE, HOWEVER, TO RETURN SLOWLY TO FULL EMPLOYMENT WHILE EXPANDING THE MANUFACTURING BASE, WITHOUT THE THREAT OF DISRUPTIONS

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P R 301106Z MAR 77
FM AMEMBASSY LONDON
TO SECSTATE WASHDC PRIORITY 2101
TREASURY DEPT WASHDC PRIORITY
INFO AMEMBASSY BONN
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ARISING FROM BALANCE OF PAYMENTS PROBLEMS. THE SECOND RELATED PROBLEM IS TO ACHIEVE HIGHER PRODUCTIVITY' AND A HIGHER LEVEL OF "NON-PRICE COMPETITIVENESS." BY WHICH IS MEANT "BETTER PRODUCT DESIGN, HIGHER QUALITY AND GREATER RELIABILITY, ALLIED TO BETTER SALESMANSHIP, DELIVERYTIMES AND SERVICING ARRANGEMENTS."

10. THE PERFORMANCE OF THE WORLD ECONOMY ASSUMES AN IM-
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PORTANT ROLE IN THE GOVERNMENT'S PLANS. IF WORLD TRADE DOES NOT GROWHFASTER THAN IT HAS AND IF BRITAIN'S SHARE IN THIS TRADE DOES NOT INCREASE, THE GOVERNMENT'S FORECASTS WILL NOT MATERIALIZE. THE CHANCELLOR, CONSEQUENTLY, SPENT SIGNIFICANT TIME REVIEWING THE WORLD ECONOMY AND URGING A COORDINATED EXPANSION OF THE INDUSTRIAL ECONOMIES. HE STATED THAT THIS CASE WOULD BE STRONGLY PRESSED OVER THE NEXT THREE MONTHS IN THE EC, THE IMF AND THE LONDON SUMMIT. HE LOOKE FORWARD AS WELL TO A REVIEW WITHIN THE EC OF EFFORTS TO RELIEVE UNEMPLOYMENT IN ANOTHER TRIPARTITE CONFERENCE OF GOVERNMENT, TRADE UNIONS AND EMPLOYERS BEFORE THE END OF JUNE.

11. OTHER MESSAGES IN THIS BUDGET SERIES INCLUDE AN OVERVIEW OF THE CHANCELLOR'S BUDGET (LONDON 5180). MAJOR FISCAL ELEMENTS IN THE BUDGET (LONDON 5182) AND BUDGET CLOSES AN EXCHANGE CONTROL LOOPHOLE (LONDON 5179).

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Message Attributes

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